



This document is scheduled to be published in the Federal Register on 11/04/2011 and available online at <http://federalregister.gov/a/2011-28601>.

**DEPARTMENT OF DEFENSE**

**BILLING CODE 5001-06**

**Office of the Secretary**

**DOD-2009-OS-0030/RIN 0790-AI45**

**32 CFR PART 165**

**Recoupment of Nonrecurring Costs (NCs) on Sales of U.S. Items**

**AGENCY:** Office of the Under Secretary of Defense (Comptroller)/Chief Financial Officer, DoD.

**ACTION:** Proposed rule

**SUMMARY:** This rule updates policy, responsibilities, and procedures to conform with section 21(e)(1)(B) of Public Law 90-629, as amended, and section 9701 of title 31, United States Code (U.S.C.), for calculating and assessing NC recoupment charges on sales of items developed for or by the Department of Defense to non-U.S. Government customers.

**DATES:** Comments must be received within [INSERT 60 DAYS FROM DATE OF PUBLICATION IN THE FEDERAL REGISTER].

**ADDRESSES:** You may submit comments, identified by docket number and/or RIN number and title, by any of the following methods:

- Federal Rulemaking Portal: <http://www.regulations.gov>. Follow the instructions for submitting comments.
- Mail: Federal Docket Management System Office, 1160 Defense Pentagon, Room 3C843, Washington, DC 20301-1160.

*Instructions:* All submissions received must include the agency name and docket number or Regulatory Information Number (RIN) for this Federal Register document. The general policy

for comments and other submissions from members of the public is to make these submissions available for public viewing on the Internet at <http://www.regulations.gov> as they are received without change, including any personal identifiers or contact information.

**FOR FURTHER INFORMATION CONTACT:** Claire Nelson, 703-602-0250.

## **SUPPLEMENTARY INFORMATION**

### **Executive Order 12866, “Regulatory Planning and Review” and Executive Order 13563 “Improving Regulation and Regulatory Review”**

It has been certified that 32 CFR part 165 does not:

- (1) Have an annual effect on the economy of \$100 million or more or adversely affect in a material way the economy; a section of the economy; productivity; competition; jobs; the environment; public health or safety; or State, local, or tribal governments or communities;
- (2) Create a serious inconsistency or otherwise interfere with an action taken or planned by another Agency;
- (3) Materially alter the budgetary impact of entitlements, grants, user fees, or loan programs, or the rights and obligations of recipients thereof; or
- (4) Raise novel legal or policy issues arising out of legal mandates, the President’s priorities, or the principles set forth in these Executive Orders.

### **Sec. 202, Pub. L. 104-4, “Unfunded Mandates Reform Act”**

It has been certified that 32 CFR part 165 does not contain a Federal mandate that may result in expenditure by State, local and tribal governments, in aggregate, or by the private sector, of \$100 million or more in any one year.

**Public Law 96-354, “Regulatory Flexibility Act” (5 U.S.C. 601)**

It has been certified that 32 CFR part 165 is not subject to the Regulatory Flexibility Act (5 U.S.C. 601) because it would not if promulgated, have a significant economic impact on a substantial number of small entities.

**Public Law 96-511, “Paperwork Reduction Act” (44 U.S.C. Chapter 35)**

It has been certified that 32 CFR part 165 does not impose reporting or recordkeeping requirements under the Paperwork Reduction Act of 1995.

**Executive Order 13132, “Federalism”**

It has been certified that 32 CFR part 165 does not have federalism implications, as set forth in Executive Order 13132. This rule does not have substantial direct effects on:

- (1) The States;
- (2) The relationship between the National Government and the States; or
- (3) The distribution of power and responsibilities among the various levels of Government.

**List of Subjects in 32 CFR Part 165**

Armed forces, Arms and munitions, Government contracts

**Accordingly 32 CFR Part 165 is revised to read as follows:**

**PART 165– RECOUPMENT OF NONRECURRING COSTS (NCS) ON SALES OF U.S.**

**ITEMS**

Sec.

165.1 Purpose.

165.2 Applicability.

165.3 Definitions.

165.4 Policy.

165.5 Responsibilities.

165.6 Procedures.

165.7 Waivers (including reductions).

**Authority:** 31 U.S.C. 9701; 22 U.S.C. 2761(e)

**§165.1. Purpose.**

This part updates policy, responsibilities, and procedures to conform with section 21(e)(1)(B) of Public Law 90-629, as amended, and section 9701 of title 31, United States Code (U.S.C.) for calculating and assessing NC recoupment charges on sales of items developed for or by the Department of Defense to non-U.S. Government customers.

**§165.2. Applicability.**

(a) This part applies to the Office of the Secretary of Defense, the Military Departments, the Office of the Chairman of the Joint Chiefs of Staff and the Joint Staff, the Combatant Commands, the Office of the Inspector General of the Department of Defense, the Defense Agencies, the DoD Field Activities, and all other organizational entities within the Department of Defense (hereafter referred to collectively as the “DoD Components”).

(b) This part does not apply to sales of excess property when accountability has been transferred to property disposal activities and the property is sold in open competition to the highest bidder.

(c) The policies and procedures in this part apply to all sales on or after the effective date of this part, and supersede application thresholds and charges previously established. Previous application thresholds and charges continue to govern sales made prior to the applicable effective date of this part. Such previously established NC recoupment thresholds and charges shall be eliminated or revised in accordance with this part.

### **§165.3. Definitions.**

Cost pool. Represents the total cost to be distributed across the specific number of units, normally the number of units produced plus those planned to be produced. The nonrecurring research, development, test, and evaluation cost pool comprises the costs described in definition for nonrecurring research, development, test and evaluation costs. The nonrecurring production cost pool comprises costs described in definition for nonrecurring production costs.

Foreign military sale. A sale by the U.S. Government of defense items or defense services to a foreign government or international organization under authority of the Arms Export Control Act (AECA); section 21(e)(1)(B) of Public Law 90-629, as amended. Except as waived by Under Secretary of Defense for Policy (USD(P)), foreign military sales are the only sales subject to NC recoupment charges.

Major defense equipment. Any item of significant military equipment on the United States Munitions List having a nonrecurring research, development, test, and evaluation cost of more than 50 million dollars or a total production cost of more than 200 million dollars. The determination of whether an item meets the major defense equipment dollar threshold for research, development, test, and evaluation shall be based on DoD obligations recorded to the date the equipment is offered for sale. Production costs shall include costs incurred by the Department of Defense. Production costs for the foreign military sales program and known direct commercial sales production are excluded.

Model. A basic alpha-numeric designation in a weapon system series; e.g., a ship hull series, equipment or system series, an airframe series, or a vehicle series. For example, the F5A and the F5F are different models in the same F-5 system series.

Nonrecurring production costs. Those one-time costs incurred in support of previous production of the model specified and those costs specifically incurred in support of the total projected production run. Those NCs include DoD expenditures for preproduction engineering; special tooling; special test equipment; production engineering; product improvement; destructive testing; and pilot model production, testing, and evaluation. That includes costs of any engineering change proposals initiated before the date of calculations of the NC recoupment charge. Nonrecurring production costs do not include DoD expenditures for machine tools, capital equipment, or facilities for which contractor rental payments are made or waived in accordance with the Defense Federal Acquisition Regulation Supplement<sup>1</sup>.

Nonrecurring research, development, test and evaluation costs. Those costs funded by a research, development, test, and evaluation appropriation to develop or improve the product or technology under consideration either through contract or in-house DoD effort. This includes costs of any engineering change proposal started before the date of calculation of the NC recoupment charges as well as projections of such costs, to the extent additional effort applicable to the sale model or technology is necessary or planned. It does not include costs funded by either procurement or operation and maintenance appropriations.

Pro rata recovery of NCs. An equal distribution (proration) of a pool of NCs to a specific number of units that benefit from the investment so that a DoD Component shall collect from a customer a fair (pro rata) share of the investment in the product being sold. The production quantity base used to determine the pro rata calculation of major defense equipment includes total production.

Significant change in NCs recoupment charge. A significant change occurs as follows:

- a. A new calculation shows a change of 30 percent of the current system NC charge.

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<sup>1</sup> Available at <http://www.acq.osd.mil/dpap/dars/dfarspgi/current/index.html>

- b. The NC unit charge increases or decreases by 50,000 dollars or more.
- c. Where the potential for a 5 million dollar change in recoupment exists.

The total collections may be estimated based on the projected sales quantities. A significant change occurs when potential collections increase or decrease by 5 million dollars.

“Special” research, development, test, and evaluation and nonrecurring production costs.

Costs incurred under a foreign military sale at the request of, or for the benefit of, a foreign customer to develop a special feature or unique or joint requirement. Those costs must be paid by the customer as they are incurred.

#### **§165.4. Policy.**

It is DoD policy that:

(a) The NC recoupment charge shall be imposed for sales of major defense equipment only as required by an Act of Congress (Section 21(e)(1)(B) of Public Law 90-629, as amended). The USD(P) may grant a waiver to recoupment charges in accordance with §165.7 of this part.

(b) The NC charges shall be based on the amount of the Department of Defense nonrecurring investment in an item.

#### **§165.5. Responsibilities.**

(a) Under Secretary of Defense (Comptroller)/Chief Financial Officer (USD(C)/CFO)) shall provide necessary financial management guidance.

(b) The Under Secretary of Defense for Acquisition, Technology, and Logistics shall take appropriate action to revise the Defense Federal Acquisition Regulation Supplement in accordance with this part.

(c) The USD(P) shall:

- (1) Monitor the application of this part.

(2) Review and approve NC recoupment charges and NC recoupment charge waiver requests received from foreign countries and international organizations for foreign military sales.

(3) Ensure publication of a listing of items developed for or by the Department of Defense to which NC recoupment charges are applicable.

(4) USD(P) may grant a waiver to recoupment charges in accordance with §165.7 of this part.

(d) The Secretaries of the Military Departments and the Directors of the Defense Agencies shall:

(1) Determine the DoD nonrecurring investment in items developed for or by the Department of Defense and perform required pro rata calculations in accordance with this part and financial management guidance from USD(C)/CFO when a military equipment asset type is considered a candidate for sale.

(2) Validate and provide recommended charges to USD(P). Supporting documentation will be retained until the item has been eliminated from the NC recoupment charge listing.

(3) Review approved NC recoupment charges on a biennial basis to determine if there has been a change in factors or assumptions used to compute a NC recoupment charge and, if there is a significant change in a NC recoupment charge, provide a recommended change to USD(P).

(4) Collect charges on foreign military sales, in accordance with DoD 7000.14-R<sup>2</sup>.

(5) Deposit collections to accounts as prescribed by USD(C)/CFO.

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<sup>2</sup> Available at <http://www.defenselink.mil/comptroller/fmr/>



(6) Request guidance from USD(P), within 90 days of issue identification, if an issue concerning a recoupment charge cannot be resolved.

**§165.6. Procedures.**

(a) The NC recoupment charge to be reimbursed shall be a pro rata recovery of NCs for the applicable major defense equipment. Recovery of NC recoupment charges shall cease upon the recovery of total DoD costs. Such charges shall be based on a “cost pool” as defined in §165.3 of this part. For a system that includes more than one component, a “building block” approach (i.e., the sum of NC recoupment charges for individual components) shall be used to determine the NC recoupment charge for the sale of the entire system.

(b) The NC recoupment charge shall not apply when a waiver for the specific customer/case has been approved by USD(P), in accordance with §165.7 of this part, or when sales are financed with U.S. Government funds made available on a non-repayable basis. Approved revised NC recoupment charges shall not be applied retroactively to accepted foreign military sales agreements.

(c) When major defense equipment is sold at a reduced price due to age or condition, the NC recoupment charge shall be reduced by the same percentage reduction.

(d) The full amount of “special” research, development, test, and evaluation and nonrecurring production costs incurred for the benefit of particular customers shall be paid by those customers. However, when a subsequent purchaser requests the same specialized features that resulted from the added “special” research, development, test, and evaluation and nonrecurring production costs, a pro rata share of those costs may be paid by the subsequent purchaser and transferred to the original customer if those special NCs exceed 50 million dollars. The pro rata share may be a unit charge determined by the DoD Component as a result of

distribution of the total costs divided by the total production. Such reimbursements shall not be collected after 10 years have elapsed since acceptance of the “Letter of Offer and Acceptance” DoD 5105.38-M<sup>3</sup>, by the original customer, unless otherwise authorized by USD(P). The U.S. Government shall not be charged any NC recoupment charges if it adopts the features for its own use or provides equipment with such features under a U.S. grant aid or similar program.

(e) For co-production, co-development and cooperative development, or cooperative production DoD agreements, the policy in this part shall determine the allocation basis for recouping from the third-party purchasers the investment costs of the participants. Such DoD agreements shall provide for the application of the policies in this part to sales to third parties by any of the parties to the agreement and for the distribution of recoupment among the parties to the agreement.

#### **§165.7. Waivers (including reductions).**

(a) Section 21(e)(10)(B) of Public Law 90-629, as amended, requires the recoupment of a proportionate amount of NCs of major defense equipment from foreign military sales customers but Section 21(e)(2) authorizes consideration of reductions or waivers for particular sales which, if made, significantly advance U.S. Government interests and the furtherance of mutual defense treaties between the United States and certain countries. Waivers may also be authorized if imposition of a NC recoupment charge likely would result in the loss of the sale; or, in the case of a sale of major defense equipment that is also being procured for the use of the Armed Forces, result in savings to the United States on the cost of the equipment procured for the Armed Forces, through a resulting increase in the total quantity of equipment purchased from the source of the equipment causing a reduction in the unit cost of the equipment, substantially offsetting the revenue foregone by reason of waiving the charge. Any increase in a NC recoupment charge

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<sup>3</sup> Available at <http://www.dsca.osd.mil/samm/>

previously considered appropriate under Section 21(e)(1)(B) may be waived if the increase results from a correction of an estimate (reasonable when made) of the production quantity base that was used for calculating the charge.

(b) Requests for waivers should originate with the foreign government and shall provide information on the extent of standardization to be derived as a result of the waiver.

(1) Blanket waiver requests should not be submitted and shall not be considered. The term “blanket waiver” refers to a NC recoupment charge waiver that is not related to a particular sale; for example, waivers for all sales to a country or all sales of a weapon system.

(2) A waiver request shall not be considered for a sale that was accepted without a NC recoupment charge waiver, unless the acceptance was conditional on consideration of the waiver request.

(3) Requests for waivers shall be processed expeditiously, and a decision normally made to either approve or disapprove the request within 60 days after receipt. A waiver in whole or in part of the recoupment charge or a denial of the request shall be provided in writing to the appropriate DoD Component.

Dated: October 31, 2011.

Aaron Siegel,  
Alternate OSD Federal Register Liaison Officer,  
Department of Defense.

[FR Doc. 2011-28601 Filed 11/03/2011 at 8:45 am; Publication Date: 11/04/2011]